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Prime Minister Matti Vanhanen
The European Union and the Challenge of Globalisation
London School of Economics
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Professor Featherstone,
Ladies and Gentlemen,
Dear Students,

It is a great honour to be here at the London School of Economics. It is actually quite a humbling experience to speak to you about globalisation. This institution has been at the cutting edge of the intellectual debate on all the important subjects of our modern age. I feel that I should be the one sitting in the audience listening to what you have to say.

Ideas are a global commodity. They travel fast and influence the very foundations of our societies. But in this age, the era of globalisation, we must also recognise the very fundamental role of economics in shaping our world. I am no Marxist, but I think that Karl Marx had a point. The economy – and economics – rule; they are what drives our world forward.

My theme for this lecture is the European Union and the Challenge of Globalisation. The founding fathers of the Union had the war fresh in their minds, a war that very few in Europe came through unscathed. However, from the very earliest days, economic motives have played a central role in moving European integration forward. I think that it is fair to say that European integration is Europe's early answer to globalisation, even though the Union predates our recent preoccupation with globalisation.

Earlier, globalisation manifested itself in the shape of multinational corporations. As I remember, this was the debate in the 1970s: how are nation states to survive as effective actors in the age of the global corporation. European integration as a political project made sense: if companies operate across borders, so should governments. Governments should pool their resources and sovereignty cross-border, if only to remain effective in the face of international companies.

Globalisation as we now know it today, as a truly worldwide phenomenon, was the result of the unprecedented opening of emerging economies to trade, investment and technology - a clear shift in the intellectual landscape with the end of the Cold War. Foreign investment on a global scale has made competition and production truly global.

For instance in Finland, we are seeing jobs and production move at an ever faster pace to low-cost countries – and low-cost markets – especially China. And we cannot be complacent and console ourselves with the thought that only low value-added jobs are at risk and that we, as affluent economies, will keep all the goodies. China and India are producing engineers and scientists by the million. Emerging economies are ever more attractive as locations for research and development. Many activities which have been considered the preserve of the developed economies may move away to distant locations.

Globalisation places huge demands on our competitiveness – there is no hiding place, no shelter from competition. This needs to be recognised by all. The days when we could contemplate visions of a Fortress Europe, a haven protected from global winds, is long past. Isolation and economic nationalism do not work in the world economy today. Not if we want to remain at its prosperous forefront.

But this needs to be said as well: globalisation is a challenge for us, but it is not a threat, nor an immoral or evil development. Globalisation can be a force for good, and it has brought benefits to the many by lifting people out of poverty. We are witnessing this in China, India and many other places. As

I have said on numerous occasions, globalisation has been the most effective development-aid project in the world.

Ladies and Gentlemen,

What is the European Union to do about globalisation? As I said, we cannot afford to ignore it, nor should we think about building higher walls against the world outside. Such responses may be understandable in a way, but they simply would not work and would actually condemn the EU to a vicious circle of lower growth and diminishing prosperity.

The first thing we can do is to cultivate our competitiveness – devote our attention to remaining competitive and improving our standing. And here we should keep in mind that the real underlying competitive strength of the EU is the internal market. This market – by many counts the largest in the world – provides European companies with a strong home market and tough competition – essential sparring partners that help keep them fit for the global market. Tough competition at home serves as a springboard for global success.

Therefore, one essential measure for European competitiveness is to take the single market further, improve it and enlarge it. For instance, a real internal market in services is crucial for Europe. Services are a vibrant sector with strong growth ahead. European companies cannot compete on the global stage if they lack the necessary foundations, which only a European internal market in services can provide. Britain is a very positive example of the importance that international services – like financial services or creative industries – can have for Europe. And many services have the added advantage that they need to be produced locally, which means jobs. Care, for instance, cannot be outsourced to foreign locations.

The Lisbon Strategy is designed to give focus to our efforts to become more competitive. We need to make tangible progress. To this end, the Finnish Presidency will organise an Informal Summit in Lahti, along the same lines as the successful Hampton Court meeting last autumn. I feel that this kind of informal discussion among leaders is a very useful way of taking things forward. I am glad that Tony Blair took this initiative during the UK Presidency. A good idea which I am now copying. I hope Tony won't mind.

At Lahti we will focus on innovation policy, because our capacity to innovate is really at the very core of our competitiveness. Companies innovate, but public policies – at EU and national level – set the scene for companies to realise their innovation potential. As I said before, we cannot compete with cheaper labour, nor can we take shelter from ever toughening competition. Instead we need to move further up the value-added chain in the world economy, find new products and new ways of making them. For this, we really depend on having an effective innovation policy that not only encourages innovations, but also turns them into cutting-edge products, companies that are world leaders in their field, and above all, good jobs for our workers. Europe's real challenge is to create a policy mix for innovation that helps translate investment in knowledge into successful products and services.

I know that innovation is hardly a crowd pleaser. No one will take to the barricades to fight for a more ambitious innovation policy. Nor will they demonstrate in the streets for more R&D funding. People are not passionate about innovation. Which is why this is a perfect theme for a Finnish EU Presidency.

As part of the Lisbon Strategy, the target for research and development expenditure has been set at 3 per cent of GDP. This reflects an important commitment to improving innovation financing. I believe that if we were to reach this target it would mean an additional R&D investment of some 100 billion euros annually, about as much as the EU budget. But that alone is not enough. It is like fixing your gaze on the thermometer instead of the weather. Innovation as an activity is above all demand-driven. We need to focus on creating market conditions conducive to innovation. If we get the market conditions right, if we produce conditions that are conducive to innovation and investment, that will deliver a lasting improvement in our ability to compete. Governments should provide good regulation and ensure healthy competition. We should also keep in mind that innovation is not just about product improvement – it includes services, marketing, logistics and new inventions. It is not limited to things,

it is also about the way we make, use and sell them. We look forward to the Commission's proposal for a European Institute of Technology to boost the European research effort.

Standards are one good example. Setting strong common European standards in mobile telephony was an essential element in turning Europe into the world leader it now is in this field. Imagine what the situation would have been if we had adopted national standards and not European ones. We would all be using a Motorola. European mobile telephony standards were so successful that they were subsequently adopted by many regions of the world. I think that we should follow this path and make sure that we have the capacity to set strong and attractive standards, standards that could become worldwide.

Unfortunately our innovation policy is still too fragmented and inefficient. Let me mention just one blatant example. After years of debate within the Council, we still have not been able to agree on a Europe-wide patent system. We are harming ourselves by our inability to agree on essential European prerequisites for innovation like this.

The pharmaceutical sector serves as a warning. In 1992, six out of ten of the top-selling pharmaceutical products in the world were produced by European companies. In 2002, this figure had dropped to two out of ten. We must do more to achieve a single market in pharmaceuticals. Further efforts to simplify legislation and regulation at EU level are badly needed.

Of course, innovation policies alone are not enough. We need to make our markets function better, which requires further reform of labour and product markets and of the public sector. Reform is never easy – at least, not if you want to win the next elections - but it is wrong to maintain that economic reform is by definition an enemy of the so-called European social model, or models to be more accurate. There is no conflict between economic efficiency and social cohesion, as Nordic economies have shown.

Neither is competitiveness an enemy of the environment. I believe that ambitious environmental policies can actually strengthen our competitiveness: clean technologies are the way of the future, so is energy efficiency. Having a market-based emissions-trading scheme in Europe is an asset. It is a practical way of dealing with climate change on a global scale.

These are examples of strategic priorities that we must get right if we are serious about competitiveness. At the beginning of the Finnish EU Presidency, I was asked to sum up our three most important priorities. My answer was innovation, innovation and innovation.

Ladies and Gentlemen,

More effective decision-making and more cohesion in external action are also essential ways of boosting the EU's ability to respond to globalisation. The Constitutional Treaty would bring welcome improvements to our decision-making and also make the EU more cohesive in terms of external representation and action. I will not go into the detail of the EU's institutional architecture, but let me say one thing: the EU needs to be effective on the global stage, because divided, we fall. Not even big European countries are big enough to make a difference in a globalising world. We have very little influence on global issues if we all choose to act on our own. This is self-evident in a place like Helsinki, but it is nevertheless also true in London, Paris, Berlin, Rome or Madrid.

We need to be able to act decisively, quickly and coherently. The Constitutional Treaty would provide many improvements, but we are not condemned to inaction without it. In fact, the EU already has one external sector, which works effectively and presents the EU as a single entity to the outside world. I am talking about trade policy, where the EU as such is a major global actor among other leading global powers. I think that we should take a lesson from our own trade policy and see whether other external policies might ideally function along the same lines, with member states being closely consulted and making the decisions, but with the EU represented by a single actor empowered to negotiate on our collective behalf. I believe that this could be a very useful model for our external relations in general.

Energy policy is a good example of a field where we could benefit from more external unity. The external dimension of energy policy will be discussed at Lahti. The EU has an internal market in energy and we need to extend the principles behind it to neighbouring producers, for the market to function properly. This is mainly about seeking a level playing field between consumers and producers, because external producers cannot expect an open EU market without reciprocity.

We are happy to buy Russian energy, and Russia needs our markets. But at the same time we need a commitment to more transparent rules in Russia, to guarantee fair treatment for foreign companies and make energy provision more predictable. EU leaders will discuss these issues with President Putin at Lahti, and this brings me back to my main point: effective external relations. Russia is a strategic partner for the EU. Now, do you think that the EU will have more influence with Russia if we act together, or as separate member states, each with our own agenda? I think that the answer is obvious.

Ladies and Gentlemen,

The enlargement of the European Union is a part of our theme here this evening – the EU and the Challenge of Globalisation.

Enlargement is benefiting the EU – both old and new member states. The accession of ten new countries has made the EU more competitive, more vibrant; it has added to the Union's weight in the world. I think that a recent Commission study demonstrated that the economic impact of the latest enlargement has been very positive.

The enlargement process continues and I am happy that Bulgaria and Romania will be joining our European family from next year.

I believe that Turkey deserves to be considered on its own merits, in the same way as any other candidate. The road to membership is never easy, and Turkey is a unique country in Europe in terms of population alone, but a Turkey that fulfils the conditions of EU-membership would benefit both the Union and Turkey.

The Finnish Presidency is actively working to ensure that Turkey proceeds with the fulfilment of her obligations under the Additional Protocol to the Ankara Agreement. A positive outcome would help us to avert difficulties with Turkey's EU accession negotiations.

We also continue to seek a solution that would enable direct trade between the European Union and the northern part of Cyprus.

We continue to talk with the Republic of Cyprus, the Turkish Cypriot Community, Turkey and other relevant actors. The following weeks will be important for these efforts as the European Commission has announced it will issue its progress report on Turkey on 8 November.

Ladies and Gentlemen,

Enlargement benefits the European economy, but at the same time enlargement is also the best security policy we have ever had. Enlargement has taken European stability to new frontiers and, with enlargement an ongoing process, this stability radiates beyond the Union's existing borders. It is living testimony to the success of European integration that so many are seeking to join the European Union.

The Western Balkans is an important example. As a European, I must say I am ashamed that we have allowed all the atrocities in the former Yugoslavia to take place, on our own continent, in our recent history. As if the last World War had taught us nothing. The horrors of Srebrenica are just little over ten years old.

I believe that the countries in the Western Balkans are heading for a European future, and even a distant prospect of EU membership has a decisive influence on the way they are re-building their societies. They need to look forward. I have personally spoken with many leaders in that region. They

all have the same message – the EU is their main partner and aspiration. Croatia has already advanced quite far in the membership process, but Bosnia-Herzegovina, Albania, Montenegro, the Former Yugoslav Republic of Macedonia, and Serbia are all potential EU members. The status of Kosovo will, I hope, be resolved soon. The countries of this region, with its tragic recent past, deserve the prospect of being part of our Europe. If they take the right path, we must meet them with open arms.

Ladies and Gentlemen,

Within the EU, there are clear signs of enlargement fatigue. First the Constitutional Treaty ran into difficulties and now some say that the EU should pause before taking in any new members. The rallying cry for this school of thought is absorption capacity. In December, the Presidency will organise a debate among EU leaders about enlargement, in line with what was decided at the June European Council. This debate is warranted, but I strongly feel that it should not lead to further conditions being set for enlargement. The EU needs results, not further reflection periods.

I have great sympathy with those who say that the Constitutional Treaty should be ratified before we take new members on board. So it should. The Constitutional Treaty provides many important improvements to the way we govern an enlarged Union. However, I cannot agree with those who think that ratification of the Constitutional Treaty should be made into a condition for further enlargement. Enlargement needs to continue, with or without the Constitutional Treaty.

We need to maintain an enlargement policy that keeps the EU open to countries that are willing and able to meet the strict and demanding conditions of membership. If we now set further conditions – conditions which are basically internal to the EU and over which potential candidates have no influence, like ratification of the Constitutional Treaty – then we risk demoralising deserving candidates, for whom the prospect of EU membership, however distant, is a strong incentive to reform and live up to European standards. This would break the strong bond that the EU has developed with its neighbours.

The current EU enlargement policy, based on objective criteria, is a true success. The last enlargement was a huge leap, taking in ten new members, but its impact has been very positive. The EU has not come to a standstill, as many opponents of enlargement predicted. I sincerely believe that Europe will benefit greatly from carrying on with enlargement. I hope that the December debate on enlargement will cement our common understanding on the policy and strengthen the consensus on enlargement.

This needs to be said loud and clear: the EU must not set new criteria for enlargement. The EU has acted as a beacon for European nations that have emerged from the shadows of the Cold War, a beacon that has encouraged both reform and modernisation. If the keepers of that beacon prevent it from shining out, there is no knowing what course the ships will take in the darkness. Our difficult and dark past haunts us still. Just last week I met Carla Del Ponte, Chief Prosecutor of the International Criminal Tribunal for the Former Yugoslavia. She told me how war criminals are still shielded from justice.

Ladies and Gentlemen,

Let me finish my speech by making a few comments about Britain in Europe. Clearly, Britain is a leader in Europe. The British EU Presidency, a year ago, managed to resolve many difficult issues that are crucial for Europe, for instance opening accession negotiations with Turkey and agreeing on the next financial framework – never an easy task.

At the same time, Britain is known for having its way of thinking about many things – things that most other EU members take for granted – like Britain not being part of Schengen, the EU's passport-free zone, and especially staying outside the Eurozone, and keeping the pound. Meanwhile, we have had the euro in our wallets for less than five years, yet using it seems the most natural thing in the world for people from Finland to Portugal.

We had a debate in Finland about joining the euro. Many felt that the Finnish economy would not perform well within the Eurozone, for example because our economy follows a cycle that is perhaps

more in tune with the United States than many other EU economies. However, sceptics – like myself - have been proved wrong by our initial experiences. Finland had an unstable currency and punitively high interest rates in the early 1990s – not unlike Britain at that time – and being in the Euro has brought unprecedented monetary stability for Finland. It is actually one of the underlying factors in our current strong economic performance. I think the early 1990s demonstrated that having a bigger economy – like Britain's – is no insurance against monetary instability.

Britain has a strong economy and a well-managed monetary policy outside the Eurozone. I have no lessons to give here. However, I feel that the euro has been one of the EU's success stories in terms of globalisation. Our companies have benefited from monetary stability and using the euro has removed one big practical obstacle to trade and economic activity within the Eurozone. The euro is a success.

It is not my place to make a judgment about British entry, but I can say that, if Britain decides to join, it will be a welcome member. And I am not saying this just because all clubs are happy to welcome wealthy and popular members.

The paradox about Britain not being in the innermost core of the Union – which the Eurozone clearly constitutes – is that in the past ten years the European Union has moved very much in the direction that Britain has long advocated: ambitious about enlargement, more open to the world and serious about economic reform. Britain clearly belongs in the political core of a union that holds these convictions close to its heart.

Thank you.